

AR 71

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Edmonton, Alberta T6G 2R6

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A N N U A L R E P O R T

**THERMAX**  
INTERNATIONAL CORP.



## A N N U A L   M E E T I N G

The Annual General Meeting of the Shareholders of Thermax International Corp. will be held on March 27, 1998 at 10 AM in the offices of Ballem MacInnes located at 1800, 350 - 7th Avenue S.W., Calgary, Alberta. All Shareholders are encouraged to attend.

## C O R P O R A T E   P R O F I L E

Thermax International Corp. carries on the business of manufacturing and selling, under license, down-hole thermosetting products to the oil and gas industry. The thermosetting products are currently used during drilling, production, workover and abandonment operations in the oil and gas industry. In addition, the Company provides technical support through its engineering personnel and its own laboratory facility. The Company is actively involved in investigating new applications for its products in the mining and seismic industries as well as applications in civil construction.

Thermax International Corp. is listed for trading on The Alberta Stock Exchange under the symbol THM.



## P R E S I D E N T ' S   M E S S A G E   T O   T H E   S H A R E H O L D E R S

On behalf of the Board of Directors, I am pleased to present the 1997 annual report to the Shareholders of Thermax International Corp.

During 1997 Thermax expanded its marketing focus beyond the Canadian petroleum industry. Thermax products were introduced to international oil and gas markets, resulting in several direct sales to a company operating in Russia. In addition, in late 1997 Thermax entered into marketing and distribution agreements with two major international oil and gas service companies actively operating in Russia. These agreements provide the Company with a solid, cost effective base to further facilitate sales into the Russian oil and gas market.

Thermax continued to broaden its exposure in the Canadian petroleum industry by adding three large pumping service companies as marketers during 1997. This now provides Thermax with a total of seven service companies to market and distribute products in the Canadian market.

Thermax's marketing strategy has also expanded to encompass new industry applications for its products. The Company is currently evaluating applications in the seismic and civil engineering industries both in Canada and Europe.

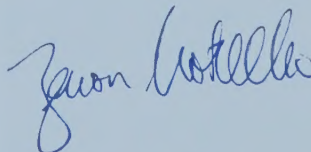
During the year ended September 30, 1997, Thermax's success in marketing beyond the Canadian petroleum industry resulted in revenues more than doubling to \$714,408.

In August of 1997 Thermax closed a \$500,000 private placement to finance ongoing marketing activities and reduce debt levels.

I would like to thank our dedicated employees for their hard work and our Board of Directors for their support and guidance during the past year. The Company regretfully advises that Mr. Fred Coles has resigned from the Board of Directors due to his expanding business commitments. Mr. Coles has been a director since the Company's inception in 1995 and made significant contributions to Thermax's growth. At the same time we welcome Mr. Mark Wayne to the Board of Directors and look forward to his guidance in the future growth of the Company.

Thermax is well positioned to build on the diversity and marketing of its products to achieve sales in new domestic and international markets during the next year.

On behalf of the Board of Directors



Zenon S. Kotelko  
President and Chief Executive Officer

January 10, 1998

## M A N A G E M E N T ' S   D I S C U S S I O N   A N D   A N A L Y S I S

The following discussion and analysis compare the financial and operating results for 1997 with those of 1996 and should be read in conjunction with the audited consolidated financial statements of Thermax for the year ending September 30, 1997.

### Sales

Sales for the year ended September 30, 1997 increased 121% from \$322,547 at September 30, 1996 to \$714,408. This increase is largely a result of the Company's sales into Russia during 1997.

### Cost of Sales

Cost of sales for the year ended September 30, 1997 were 47% of sales compared to the 1996 ratio of 74%. This reduction in the percentage of cost of sales to sales produced a gross margin that increased from 26% in 1996 to 53% in 1997. The increased margin is due to the increase in sales, staff changes and operating efficiencies.

### Administrative Expenses

These expenses increased from \$304,148 in 1996 to \$411,355 in 1997, but as a percentage of sales the administrative expenses were reduced in 1997 to 58% of sales from 94% of sales. The actual dollar increase is the result of increased operations and marketing. The percentage decline is due to management's intent to keep costs as low as possible without slowing the Company's growth.

### Interest Expense

Interest costs in 1997 decreased 44% from \$8,717 in 1996 to \$4,868. The decrease is due to a lower average cost of debt and reduced bank indebtedness in 1997.

### Working Capital

The net working capital position increased from (\$17,810) at September 30, 1996 to \$259,095 at September 30, 1997. The increase in working capital is a result of increased sales and a \$500,000 private placement (raising \$287,500 in cash and converting \$212,500 of shareholder loans to equity) which closed in August of 1997.

### Shareholder and Related Party Loans

The shareholder loans decreased from \$200,000 at September 30, 1996 to nil at September 30, 1997. The loans were partially repaid in cash and the remainder were converted to equity as part of the private placement in August of 1997.

### Share Capital

Share capital increased \$528,141 (2,325,000 shares) at September 30, 1997 as a result of a private placement and the exercise of options.



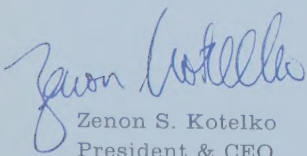
## MANAGEMENT'S REPORT

The accompanying financial statements of the Company have been prepared by management in accordance with generally accepted accounting principles and the financial and operating information presented throughout this annual report is consistent with that which is shown in the financial statements.

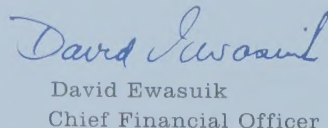
Management has developed and maintains systems of internal accounting controls, policies and procedures in order to provide reasonable assurance as to the reliability of the financial records and the safeguarding of assets.

External auditors appointed by the Shareholders of the Company have examined the financial statements and have expressed an opinion on the statements.

The Board of Directors of the Company has established an Audit Committee to review these statements with management and the auditors. The Audit Committee has approved these statements on behalf of the Company's Board of Directors.

  
Zenon S. Kotelko  
President & CEO

January 10, 1998

  
David Ewasuik  
Chief Financial Officer

January 10, 1998

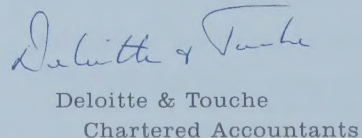
## AUDITORS' REPORT

To the Shareholders of  
THERMAX INTERNATIONAL CORP.:

We have audited the consolidated balance sheet of Thermax International Corp. as at September 30, 1997 and the consolidated statements of loss and deficit and changes in financial position for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at September 30, 1997 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

  
Deloitte & Touche  
Chartered Accountants

Calgary, Alberta.  
November 7, 1997

# CONSOLIDATED BALANCE SHEET

September 30, 1997

	1997 \$	1996 \$
<b>ASSETS</b>		
<b>CURRENT</b>		
Cash	186,071	8,317
Accounts receivable	50,711	121,984
Inventory	88,819	54,075
Prepaid expenses	2,000	6,025
	327,601	190,401
Intangible assets (note 5)	245,921	333,949
Equipment (note 6)	31,830	51,439
	605,352	575,789
<b>LIABILITIES</b>		
<b>CURRENT</b>		
Bank indebtedness (note 7)	—	30,000
Accounts payable and accrued liabilities	58,940	149,550
Due to related company	1,266	19,141
Current portion of obligation under capital lease	8,300	9,520
	68,506	208,211
Obligation under capital lease	—	8,310
Shareholder and related party loans	—	200,000
	68,506	416,521
<b>SHAREHOLDERS' EQUITY</b>		
Share capital (note 8)	1,300,536	772,395
Contributed surplus	273,959	273,959
Deficit	(1,037,649)	(887,086)
	536,846	159,268
	605,352	575,789

Approved by the board:

David Juwayil, Director

Jason Antille, Director

CONSOLIDATED STATEMENT OF LOSS & DEFICIT  
Year ended September 30, 1997

	1997 \$	1996 \$
SALES	714,408	322,547
COST OF SALES	334,798	237,339
GROSS MARGIN	379,610	85,208
EXPENSES		
Administrative	411,355	304,148
Amortization and depreciation	113,950	104,351
Interest	4,868	8,717
	530,173	417,216
NET LOSS	(150,563)	(332,008)
DEFICIT, BEGINNING OF YEAR	(887,086)	(555,078)
DEFICIT, END OF YEAR	(1,037,649)	(887,086)
LOSS PER SHARE (note 12)	(0.02)	(0.05)



CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION  
Year ended September 30, 1997

	1997 \$	1996 \$
<b>NET INFLOW (OUTFLOW) OF CASH RELATED TO THE FOLLOWING ACTIVITIES</b>		
<b>OPERATING</b>		
Net loss	(150,563)	(332,008)
Items not affecting cash flow		
Loss on disposal of equipment	-	258
Amortization and depreciation	113,950	104,351
	(36,613)	(227,399)
Changes in non-cash operating working capital items (note 10)	(67,931)	(10,258)
	(104,544)	(237,657)
<b>INVESTING</b>		
Purchase of equipment	(6,313)	(7,105)
Proceeds on disposal of fixed assets	-	525
	(6,313)	(6,580)
<b>FINANCING</b>		
Repayment of shareholder and related party loans	(59,865)	(83,752)
Advances from shareholders and related parties	72,365	95,350
Conversion of shareholder and related party loans to common shares	(212,500)	-
Issue of common shares (net of issue costs of \$4,359; 1996 - \$0)	528,141	76,667
Issue of common shares on acquisition of Thermo Star Products Limited (net of issue costs of \$6,289) (note 3)	-	318,045
Repayment of financing under obligation under capital lease	(9,530)	(8,130)
Decrease in loan payable	-	(152,209)
	318,611	245,971
<b>NET CASH INFLOW</b>	207,754	1,734
<b>CASH POSITION, BEGINNING OF YEAR</b>	(21,683)	(23,417)
<b>CASH POSITION, END OF YEAR</b>	186,071	(21,683)
Represented by:		
Bank indebtedness	-	(30,000)
Cash	186,071	8,317
	186,071	(21,683)

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Year ended September 30, 1997

### 1. CONTINUING OPERATIONS

The consolidated financial statements have been presented using accounting principles applicable to a going concern, which assume that the Company will continue in operation in the foreseeable future and be able to realize assets and satisfy liabilities in the normal course of business.

The Company's continuation as a going concern is dependent upon its ability to generate profitable operations sufficient to meet its obligations as they become due.

The consolidated financial statements do not include any adjustments to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary, should the Company be unable to continue as a going concern.

### 2. DESCRIPTION OF BUSINESS

The Company carries on the business of manufacturing and selling, under license (see note 5), down-hole thermosetting products to the oil and gas industry. The thermosetting products are currently used during drilling, production, workover and abandonment operations in the oil and gas industry. In addition, the Company provides technical support through its engineering personnel and its own laboratory facility. The Company is actively involved in investigating new applications for its products in the mining and seismic industries as well as applications in civil construction.

### 3. ACQUISITION AND BASIS OF PRESENTATION

On April 19, 1996, the Company completed a major transaction whereby it acquired all of the outstanding common shares of Thermo Star Products Ltd. (TSPL), a private company. Under the terms of the transaction, the shareholders of TSPL received two and one half common shares of the Company for each share of TSPL tendered (1,711,982 shares in total). The result is that the former shareholders of TSPL acquired in excess of 50% of the outstanding common shares of the Company.

As former shareholders of TSPL held in excess of 50% of the outstanding shares of the Company subsequent to these transactions, the business combination of the two companies has been accounted for as a reverse takeover of the Company by TSPL.

Application of reverse takeover accounting results in the following:

- a) The consolidated financial statements of the combined entities are issued under the name of the legal parent (the Company) but are considered a continuation of the financial statements of the legal subsidiary (TSPL);
- b) As TSPL is deemed to be the acquirer for accounting purposes, its assets and liabilities are included in the consolidated financial statements at their historical carrying values in the accounts of TSPL;

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS [CONTINUED]

- c) Control of the net assets and operations of the Company is deemed to be acquired by TSPL. For the purposes of this transaction, the deemed consideration is the \$324,334 ascribed to the 4,450,000 common shares of the Company outstanding when the agreement was signed. Accordingly, the common shares were recorded in the records of the Company for the deemed consideration less issue costs of \$6,289.

The accounting for the business combination on this basis can be summarized as follows:

	\$
Deemed consideration	324,334
Assigned value of net assets of the Company	
Current assets	343,662
Current liabilities	(19,328)
	324,334
Excess of deemed consideration over net assets acquired.	-

4. SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared in accordance with generally accepted accounting principles and include the following significant accounting policies:

- a) INVENTORY. Inventory is recorded at the lower of cost and net realizable value.
- b) EQUIPMENT. Equipment is recorded at cost. Depreciation is computed using the declining-balance method, at a rate of 20% for office equipment and 30% for computer and lab equipment. Lab equipment under capital lease is amortized on a straight-line basis over the lease term.
- c) LICENSED TECHNOLOGY. The licensed technology is amortized on a straight-line basis over five years, which is the term of the license. Any renewal costs will be amortized over the renewal period to which the costs relate.
- d) DEFERRED COSTS. Deferred costs capitalized during the Company's pre-operating stage are amortized on a straight-line basis over 15 years from the commencement of commercial operations on October 1, 1993.
- e) MEASUREMENT UNCERTAINTY. The preparation of financial statements in conformance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

## 5. INTANGIBLE ASSETS

	Cost	Accumulated Amortization	1997 Net Book Value	1996 Net Book Value
	\$	\$	\$	\$
Licensed technology	356,212	295,349	60,863	132,095
Deferred costs	248,272	66,208	182,064	198,615
Other	3,671	677	2,994	3,239
	608,155	362,234	245,921	333,949

The Company has entered into an exclusive licensing agreement for the manufacturing and marketing rights for Thermax products for the majority of the world.

The licensing agreement had an initial term of five years which expires on March 25, 1998 and is renewable by TSPL for successive five year renewal periods. The renewal fee for the first five year renewal (effective March 26, 1998 to March 25, 2003) of \$125,000 is due prior to March 26, 1998. The renewal fee payable by TSPL for each subsequent renewal period is an amount equal to five percent of the average net profits of TSPL for the three calendar years immediately preceding each renewal date.

## EQUIPMENT

	Cost	Accumulated Depreciation	1997 Net Book Value	1996 Net Book Value
	\$	\$	\$	\$
Lab equipment	30,134	17,463	12,671	13,935
Office equipment	12,106	5,632	6,474	7,943
Computer equipment	17,048	10,189	6,859	9,587
Lab equipment under capital lease	29,960	24,134	5,826	19,974
	89,248	57,418	31,830	51,439

## BANK INDEBTEDNESS

The Company has available a revolving demand loan in the amount of \$50,000 of which nil (1996 - \$30,000) was drawn as at September 30, 1997. Interest is charged at a rate of prime plus 1.5% per annum. The loan is secured by shareholder guarantees and an insurance plan.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

## 8. SHARE CAPITAL

	Number of Common Shares	\$
Authorized		
Unlimited number of common voting shares		
Unlimited number of preferred non-voting shares		
Issued		
As at April 19, 1996	4,450,000	324,334
Shares issued to acquire TSPL	4,279,956	454,350
Expenses of issuing shares	-	(6,289)
Balance as September 30, 1996	8,729,956	772,395
Issued upon exercise of option at \$0.10 per share	325,000	32,500
Private placement at \$0.25 per share	2,000,000	500,000
Expenses of issuing shares	-	(4,359)
Balance at September 30, 1997	11,054,956	1,300,536

## Stock Options

At September 30, 1997, the Company has granted stock options for common shares to certain directors, officers and employees entitling them to purchase 600,000 shares at prices ranging from \$0.10 to \$0.40 per share and expiring from October 1, 1999 to July 24, 2001.

## 9. INCOME TAXES

The Company has loss carryforwards of approximately \$780,000 which are available to offset taxable income. The first of these losses expire in 2001. No recognition has been given in these financial statements to the potential tax benefits which may result from these losses.

## 10. CHANGES IN NON-CASH OPERATING WORKING CAPITAL ITEMS

	1997 \$	1996 \$
Accounts receivable	71,273	2,685
Inventory	(34,744)	36,188
Prepaid expenses	4,025	(1,725)
Accounts payable and accrued liabilities	(90,610)	(30,661)
Due to related company	(17,875)	(16,745)
	(67,931)	(10,258)

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

### 11. RELATED PARTY TRANSACTIONS

During the year, the Company purchased goods in the amount of \$23,491 (1996 - \$38,101) from a company in which a director and major shareholder has a controlling interest. These transactions were made on the same terms and conditions as purchases from unrelated companies.

### 12. LOSS PER SHARE

Loss per share has been calculated using the weighted average number of common shares of the Company actually outstanding during the respective fiscal period. Fully diluted loss per share is not presented because of its anti-dilutive nature.

### 13. COMPARATIVE FIGURES

Certain of the prior year's figures have been reclassified to conform to the current year's presentation.

### 14. FINANCIAL INSTRUMENTS

The carrying value of the Company's financial assets and liabilities, which are accounts receivable and accounts payable respectively, are not materially different from their fair value due to the near term nature of these assets and liabilities.

There are no significant interest rate or concentration of credit risk associated with these assets and liabilities.



OFFICERS AND  
DIRECTORS

BOARD OF DIRECTORS

Zenon S. Kotelko  
Calgary, Alberta

David M. Ewasuik  
Calgary, Alberta

Andrew W. Kramchynski  
Calgary, Alberta

Mark Wayne  
Calgary, Alberta

Richard G. Patey  
Calgary, Alberta

OFFICERS

Zenon S. Kotelko, President & CEO  
David M. Ewasuik, Chief Financial Officer  
William DeJong, Secretary

CORPORATE INFORMATION

OFFICES

Suite 800, 605 5th Avenue S.W.  
Calgary, Alberta T2P 3H5  
Phone: (403) 232-1184 Fax: (403) 265-2893

BANKERS

Royal Bank of Canada. Calgary, Alberta

AUDITORS

Deloitte & Touche. Calgary, Alberta

REGISTRAR & TRANSFER AGENT

CIBC Mellon Trust Company. Calgary, Alberta

SOLICITORS

Ballem MacInnes. Calgary, Alberta

STOCK EXCHANGE LISTING

The Alberta Stock Exchange.  
Stock Symbol: THM

